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C O N F I D E N T I A L SECTION 01 OF 03 BAGHDAD 001366

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SUBJECT: REPORTS OF ZAIN'S IMMINENT DEMISE ARE GREATLY
EXAGGERATED

Classified By: Charles P. Ries for Reasons 1.4(b) and (d).

¶1. (C//REL MCFI) SUMMARY: Several former USG officials and some non-mainstream media reports have claimed that Zain, Iraq's leading mobile telecommunications operator, risks the collapse of its network infrastructure on May 14, 2008, if it fails to conclude negotiations with its private security contractor. The reports have also asserted that a Zain network breakdown would create dire consequences for Embassy Baghdad and the Coalition, some of whose personnel utilize Zain's services. A former Embassy Baghdad official now involved in the dispute as a private consultant has, however, informed Econoffs that: (a) Zain's differences with its security contractor are in fact a sideshow to buyout negotiations between Zain's majority and minority shareholders; (b) the shareholders would likely resolve their dispute before any ill befell Zain's network; and (c) parties with financial interests in the outcome of the negotiations have fed the Washington interagency and the media a doomsday scenario of Zain's collapse to goad the USG into pressuring the firm's majority shareholders into making concessions to their junior partners.

¶2. (C//REL MCFI) SUMMARY CONTINUED: Post assesses as low the risk that the shareholders would allow their disagreements to deteriorate such that the very investment over which they are arguing would be damaged and devalued. Multi-National Corps Iraq (MNC-I) has analyzed the potential fallout for the Coalition of a Zain network collapse and judged that our forces would have sufficient communications redundancy to manage any degradation in Zain's service. Post has advised and reiterated to the interested parties, as well as relevant GOI counterparts, that the USG and the Coalition: (a) take no particular position in this dispute, which is a private matter to be resolved by the parties themselves; (b) encourage the parties to resolve their differences quickly, amicably, peacefully, and within the bounds of Iraqi law; and (c) are not represented by the former Embassy Baghdad official involved in the negotiations as a private consultant. END SUMMARY.

THE HISTORY OF THE ZAIN SHAREHOLDER DISPUTE

¶3. (C//REL MCFI) Zain used to do business in southern Iraq as MTC Atheer pursuant to a regional license granted by the Coalition Provisional Authority (CPA) in 2004. MTC Atheer was owned 31 percent by its parent company, MTC Kuwait, 31 percent by the Kuwaiti Kharafi Group, and 38 percent by the Iraq-based Dijla Group. MTC Kuwait is a leading regional mobile telecommunications firm with subsidiary companies throughout the Middle East. After MTC Atheer won a nationwide Iraq mobile telecommunications operator license for USD 1.25 billion in September 2007, its parent company, MTC Kuwait, bought the Karafi Group's 31 percent stake,

establishing itself as majority shareholder in MTC Atheer. MTC Atheer subsequently acquired for USD 1.2 billion the assets of the CPA-licensed central Iraq regional operator, Iraqna. (NOTE: Iraqna bowed out of the bidding for a nationwide license at the September 2007 auction. END NOTE.) MTC Kuwait, and by extension its subordinate companies, at the same time began the process of re-branding themselves as "Zain."

¶4. (C//REL MCFI) Post understands that the Dijla Group contributed little to no capital to MTC Atheer at its inception in 2004, nor did it help pay for the nationwide license or the Iraqna acquisition. Instead Dijla--a family holding company with diverse commercial interests throughout Iraq--contributed as an MTC Atheer, and later Zain-Iraq, shareholder its personal connections to the GOI and its management of a security contract with the Iraq-based Babylon Eagles Security Company (BESC). A leading Dijla Group investor, Mudhar al-Shawkat, is also BESC's CEO. BESC has provided mobile security for the firm's personnel, as well as static security for its Iraq telecommunications infrastructure: towers, antennas, base stations, generators, and the like. Providing static security for such infrastructure in Iraq requires more than posting guards: BESC oversees a network of relationships with tribal sheikhs and other power brokers to ensure the infrastructure goes unmolested.

¶5. (C//REL MCFI) Tensions between Zain-Kuwait--now the majority shareholder of Zain-Iraq--and the Dijla Group began to surface in late 2007: the Dijla Group complained that Zain-Kuwait bought out the Karafi Group without properly notifying Dijla, in violation of their shareholder agreement. Zain-Kuwait also, according to the Dijla Group,

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unilaterally cancelled BESC's contract with Zain-Iraq in December 2007, likewise allegedly contravening the shareholder agreement. The Dijla Group claims that it has been paying BESC's estimated 7,000-strong guard force out of its own pocket since December 2007 and that Zain owes it roughly USD 12 million for this expenditure. Several months ago, Zain-Iraq contracted Peak Security--a firm which also provides services to the Defense Department's Task Force for Business Stability Operations (TFBSO)--to provide some of its security needs. A standoff between BESC and Peak personnel had to be mediated by the GOI Ministry of Interior with MNF-I support. Tensions mounting, the parties entered into buyout negotiations in early 2008, as well as arbitration in the United Kingdom.

ENTER SOME FORMER USG OFFICIALS

¶6. (C//REL MCFI) In mid-April 2008 the Dijla Group hired a former Embassy Baghdad official (the "ex-Emboff") as a private consultant to represent them in their ongoing negotiations with Zain-Iraq's majority shareholders. (COMMENT: The ex-Emboff is therefore not an independent mediator, but has direct business ties to one of the parties to this dispute. His comments should be seen in that light. END COMMENT.) The ex-Emboff--until March 2008 the senior consultant to the Ministry of Communications in the Embassy's Iraq Transition Assistance Office (ITAO)--began contacting former colleagues at the State Department in Washington, as well as here in Embassy Baghdad and MNF-I, warning that the shareholder dispute could sour and imploring the USG to intervene. He shared with us his grim assessment of the potential downside risks if the negotiations deteriorated and the Dijla Group ordered BESC off the job, as they have at times threatened to do: Coalition communications capabilities badly degraded, intelligence gathering and kinetic operations compromised, severe economic disruption, and social unrest leading to political instability. Econoffs and colleagues

at the Department advised him: (a) that the USG takes no particular position in this dispute, which is a private matter to be resolved by the parties themselves; (b) that the USG encourages the parties to resolve their differences quickly, amicably, peacefully, and within the bounds of Iraqi law; and (c) that he must not in his private capacity hold himself out as representing the USG, Embassy Baghdad, MNF-I, or the Coalition.

17. (C//REL MCFI) The ex-Emboff came to Iraq on or about April 22, and Econoffs met with him at the Rasheed Hotel on April 24 to discuss the matter. He advised us then that the essence of the dispute was not whether the majority shareholders paid Dijla Group for its outlays to BESC, but rather the sum of money the Dijla Group would receive for its stake in Zain-Iraq: the majority shareholders have offered USD 250 million, and the Dijla Group has countered with USD 1.2 billion. The ex-Emboff said Dijla assessed the fair market value of its stake in Zain at roughly USD 500 million. He said Zain-Iraq CEO Ali Dahwi told him the USD 12 million for BESC was of little importance to the overall dispute; Zain-Iraq would eventually pay BESC and likely hire its employees to handle static security anyway. Given the complicated tribal relationships involved, Zain could not replace BESC's employees with those of another firm.

18. (C//REL MCFI) The ex-Emboff said he believed the parties would reach an amicable resolution before any tensions resulted in violence against Zain personnel or infrastructure, a threat that has lingered in the background of the negotiations. He admitted that his rhetoric in describing this matter to the Embassy, State Department officials in Washington, and MNF-I was designed to attract high-level USG attention. He claimed that the parties have told him that USG involvement in the dispute would help them finalize an agreement: "involvement" would entail high-level Embassy or MNF-I officials contacting the parties and encouraging them to resolve the dispute quickly, amicably, and peacefully, for the sake of Iraqi and Coalition interests in a well functioning mobile telecommunications industry. Econoffs noted that we had already advised relevant interested parties--Ali Dahwi, Minister of Communications Jassim Mohammed Jafar, and representatives of the Communications and Media Commission that the USG: (a) takes no particular position in this dispute; (b) encourages the parties to resolve this dispute quickly, peacefully, and within the bounds of Iraqi law; and (c) is not represented by the ex-Emboff in any way.

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19. (C//REL MCFI) The ex-Emboff admitted that that the tone of his messages and presentations regarding the potential risks of the negotiations souring was meant to excite USG interest in intervening in the dispute, but he nevertheless stood by his technical assessment of the worst case scenario. He said that security ministries in the GOI, as well as other mobile telecommunications firms, leased space for their own antennas on Zain-Iraq's towers; BESC abandoning the infrastructure or, worse, interdicting it themselves (another lingering threat), could thus degrade service not only for Zain-Iraq, but also for, e.g., Iraq's other mobile telecommunications operators, the MOD, and the MOI. (NOTE: MNC-I has analyzed its downside risks in the unlikely event that the infrastructure collapsed and assessed that Coalition forces would have sufficient communications redundancy to manage any degradation in the services they get from Zain-Iraq. END NOTE.)

110. (C//REL MCFI) The ex-Emboff told us that a group of other former USG officials was trying to draw attention to the shareholder dispute throughout the Washington interagency with messages painting a doomsday scenario that made his own stylized assessment look "tepid" by comparison. The ex-Emboff reluctantly admitted that he

was not "guiltless" in providing this group of ex-officials with "inputs" for their Washington engagement. He also said that members of the group had "financial interests" in the outcome of the negotiations. In a subsequent conversation he admitted to Econoff his disappointment that his ex-USG Washington-based contacts had not heeded his advice to strike some of the more incendiary parts of their messages to the Washington interagency. He was concerned that their "analysis" was so histrionic that it would lack credibility and undermine his own efforts to draw the USG into the dispute.

ONGOING ENGAGEMENT ON THE MATTER

¶11. (C//REL MCFI) Post continues to cooperate with MNF-I and MNC-I to monitor the matter, assess the risks, and reach out to the interested parties and our GOI counterparts. With the assistance of Embassy Kuwait, we have communicated our position to Zain-Kuwait's Chairman Saad al-Barrak, who welcomed the clarification and appreciated the USG's position. We also have reiterated our position and encouraged the Minister of Communications and the CMC to take an active interest in ensuring that their mobile telecommunications licensee dutifully performs its responsibilities to deliver reliable service to the Iraqi people. The Embassy Economic Counselor also attended the Tuesday, April 29, meeting of Ahmed Chalabi's services committee to reiterate and clarify the USG position to that forum; Chalabi had invited the ex-Emboff to address his committee on the matter. In coordination with Post, MNF-I STRATOPS has also contacted the MOI to ensure that they are aware of the potential risks. For its part, the MOI has advised us that it is aware of the dispute, likewise assesses the risk to Zain's system as low, and stands ready to enforce the law should a genuine threat to Zain's personnel or infrastructure materialize.

¶12. (C//REL MCFI) COMMENT: It is unfortunate that a shareholder dispute generated fleeting tensions between armed security forces and veiled threats of violence against person and property. It is also unfortunate that one party has tried to prod the USG into intervening in what is a strictly private commercial matter. More welcome, however, has been the GOI's willingness--thus far--to strike a moderate stance and not reflexively wade into a private sector dispute. If Zain's shareholders resolved their dispute through negotiation and arbitration, and without government intervention, it would be a positive example of maturation for Iraq's private and public sectors. Investors would see that Iraqi shareholder disputes do not necessarily lead to mafia-style or statist "solutions." Post, MNF-I, and the MOI believe this to be the more likely outcome. If the parties did lurch toward the worst case scenario, however, Post and MNF-I will be ready to support the MOI in its mission to protect Iraq's communications infrastructure.
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